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¶1. (SBU) Summary: Conoco Philips has decided to sell its assets in Ecuador. Conoco acquired several production and exploration blocks in Ecuador when it purchased Burlington Resources in 2006, and concluded that the Ecuadorian assets are not economically attractive compared to other holdings in its portfolio. With Conoco's departure, City Oriente is the last U.S.-owned operating oil company in Ecuador (of the two other remaining U.S. companies, one produces natural gas and the other is a portfolio investor). End Summary.

¶2. (SBU) Herb Vickers, General Manager of Burlington Resources Ecuador (acquired by major oil company Conoco Phillips in May 2006) informed the Ambassador on May 10 that Conoco has decided to dispose of its assets in Ecuador. Conoco had tried to privately arrange a purchase with some of its business partners in Ecuador, but those partners backed out. Conoco will now open a data room so potential buyers can review its assets. Conoco informed the GOE of its plans, and wanted to advise the Embassy as well.

¶3. (SBU) Conoco has minority shares in two blocks in Ecuador currently producing oil (Blocks 7 and 21), which are operated by the French company Perenco. Conoco also holds the rights to two exploration blocks (Block 24 is wholly owned and Block 23 is owned jointly with Argentine firm CGC). Both exploration blocks have been in force majeure for years due to problems with indigenous and environmental groups opposed to petroleum operations.

¶4. (SBU) Vickers explained that a large petroleum company like Conoco requires a high rate of return for its assets, and the holdings in Ecuador would be hard pressed to reach that threshold. Returns in Ecuador deteriorated with the revenue sharing requirements imposed by the 2006 amendment to the Hydrocarbon Reform Law. Further complicating the equation is uncertainty regarding additional changes that might be imposed by the Correa administration, which, when incorporated into estimates of future returns, further reduce the financial attractiveness of the Ecuadorian holdings.

¶5. (SBU) Conoco first attempted to sell its assets in Ecuador to Perenco, which was interested and close to finalizing a sale in December 2006. Perenco said that it backed out of the purchase because it did not want to take on the exploration blocks that Conoco was trying to sell as port of the package. However, Vickers speculates that Perenco withdrew due to uncertainty over the direction the new Correa government might take. (Other sources ascribe Perenco's non-interest to the death of the French owner in a December 2006 French Alps skiing accident, and his heirs' desire to

sell their Ecuadorian operation.)

¶6. (SBU) Vickers said Conoco tried to package the production and exploration blocks together, so that the buyer would take over a $1 million guarantee that the company might have to pay if it abandons the exploration blocks. However, when Conoco opens a data room for its assets, it will no longer try to sell all its blocks as a package, but would be willing to give away the exploration blocks to any interested company. Vickers said that there is interest from Ecuadorian operators for the production blocks, but little interest in the exploration blocks due to the difficulties with indigenous and environmental interests. Vickers speculated that the government might cancel its exploration rights, rather than see a different company attempt to explore the area, given Energy Minister Acosta's statements that he wants to limit new exploration. If so, that would also cancel Conoco's guarantee.

¶7. (SBU) Vickers said that Conoco is framing its departure as a financial decision following the consolidation of Conoco's and Burlington's assets. Given Conoco's other holdings in the region, particularly Peru where indigenous groups also oppose its activities, Conoco does not want to give any public play to the political uncertainty that went into its calculations or the indigenous problems that also have hampered its operations. However, Vickers speculated that the international NGO community will paint Conoco's departure as a win for environmentalists.

¶8. (SBU) Comment. Ecuador's difficult and uncertain investment climate, particularly in the petroleum sector, was an important factor behind the Conoco decision to withdraw and explains its inability even to give its exploration rights gratis to another oil company. This is the second time it has left (it also pulled out in the early 1990s), rejoining the list of U.S. companies that have left Ecuador (among those that have left in the last 15 years: ARCO, Exxon, Maxus, Occidental, Tenneco, Texaco, Unocal, and Vintage). Vickers, who also worked in Indonesia, said that Indonesians kept pressing for more benefits from foreign oil companies, but knew not to push the foreign investors over a line that would force them to leave. Ecuador, he said, does not know where that line is.

¶9. (SBU) With Conoco/Burlington's withdrawal, U.S. participation in Ecuador's oil and gas sector is confined to City Oriente, EDC (Noble Energy), and Murphy Oil. City Oriente, a small, family-operated company, is the sole U.S.-owned company producing oil in Ecuador. City, like Conoco, is worried about its ability to maintain its Ecuador operation and has filed for international arbitration over the conditions imposed unilaterally by the hydrocarbons law. Noble Energy produces natural gas in offshore Block 3 to supply their electricity generator, Machala Power. Noble Energy has filed for international arbitration to recover $60m owed by the GOE for electricity sold. Murphy Oil, based in El Dorado, Arkansas, is a 20% portfolio investor in Repsol YPF's Block 16. Income from Murphy Oil's share of production fell from $7.7m in 2006 to $4.1m in 2007 due to increased royalty payments mandated in a 2006 amendment to Ecuador's Hydrocarbons Law.

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